

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

AMEREN ILLINOIS COMPANY)	
d/b/a Ameren Illinois)	
Petitioner)	Docket No. 12-0293
)	
Rate MAP-P Modernization Action Plan -)	
Pricing Filing)	

DIRECT TESTIMONY OF MICHAEL L. BROSCHE

ON BEHALF OF THE

PEOPLE OF THE STATE OF ILLINOIS

and AARP

DATED July 3, 2012

PUBLIC VERSION

DIRECT TESTIMONY OF MICHAEL L. BROSCH

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EXHIBIT LIST

AG/AARP Exhibit No. 1.1	Summary of Qualifications
AG/AARP Exhibit No. 1.2	Prior Testimony Listing
AG/AARP Exhibit No. 1.3	AG/AARP Summary of Adjustments
AG/AARP Exhibit No. 1.4	Ameren's Response to AG 3.01 and RMP 1.01 from Docket No. 12-0001 (Confidential)
AG/AARP Exhibit No. 1.5	Excerpts of Brosch CWC Testimony, Dkt. 12-0001
AG/AARP Exhibit No. 1.6	Ameren's Response to AG 2.12, AG 3.03, AG 3.02, and AG 3.05
AG/AARP Exhibit No. 1.7	Ameren's Responses to AG 2.04
AG/AARP Exhibit No. 1.8	Ameren's Responses to AG 3.10
AG/AARP Exhibit No. 1.9	Ameren's Responses to AG 3.13

I. INTRODUCTION / SUMMARY

1 **Q. Please state your name and business address.**

2 A. My name is Michael L. Brosch. My business address is PO Box 481934, Kansas
3 City, Missouri 64148-1934.

4
5 **Q. By whom are you employed and in what capacity?**

6 A. I am a principal in the firm Utilitech, Inc., a consulting firm engaged primarily in
7 utility rate and regulation work. The firm's business and my responsibilities are
8 related to regulatory projects for utility regulation clients. These services include
9 rate case reviews, cost of service analyses, jurisdictional and class cost allocations,
10 financial studies, rate design analyses, utility reorganization analyses and focused
11 investigations related to utility operations and ratemaking issues.

12 **Q. On whose behalf are you appearing in this proceeding?**

13 A. I am appearing on behalf of the People of the State of Illinois represented by the
14 Attorney General, ("Attorney General" or "AG") and AARP.

15 **Q. Will you summarize your educational background and professional experience**
16 **in the field of utility regulation?**

17 A. Yes. AG/AARP Exhibit No. 1.1 is a summary of my education and professional
18 qualifications. I have testified before utility regulatory agencies in Arizona,
19 Arkansas, California, Florida, Hawaii, Illinois, Indiana, Iowa, Kansas, Michigan,
20 Missouri, New Mexico, Ohio, Oklahoma, Texas, Utah, Washington, and Wisconsin
21 in regulatory proceedings involving electric, gas, telephone, water, sewer, transit,
22 and steam utilities. A listing of my previous testimonies in utility regulatory
23 proceedings is set forth in AG/AARP Exhibit No. 1.2. In Illinois, I have testified in

several major proceedings before the Illinois Commerce Commission (“the Commission” or “the ICC”). These include Peoples Gas rate cases in Docket Nos. 90-0007 and 07-0241, North Shore Gas Company Docket No. 92-0242, Illinois Bell Telephone Company in Docket Nos. 92-0448 and 92-0239, ComEd rate case Docket Nos. 07-0566 and 10-0467 and Ameren Illinois Utilities Docket Nos. 07-0585 through 07-0590. I also testified in ComEd Docket No. 09-0263 involving the Advanced Metering Infrastructure Pilot Program and Associated Tariffs, in response to ComEd’s alternative regulation proposal that was filed in Docket No. 10-0527, and in the pending ComEd formula rate case, Docket No. 11-0721. Most recently I testified in the initial formula rate case proceedings for ComEd and Ameren Illinois, Docket Nos. 11-0721 and 12-0001, respectively.

Q. What is the purpose of your testimony in this docket?

A. My testimony is responsive to the formula rate regulatory proposals and revenue requirement calculations of Ameren Illinois Utilities (“Ameren”, “AIC” or “Company”) that are sponsored by various AIC witnesses and are summarized in Ameren Exhibit 1.1. The January 1, 2013 rates will include (1) a prospective revenue requirement for 2013 rate year based on FERC Form 1 inputs for 2011 plus projected net plant additions for 2012. I will describe my understanding of formula rate regulation, as specified in new Section 16-108.5 of the Public Utilities Act (“PUA” or “the Act”), and then will discuss why certain of AIC’s specific proposals for formula rate regulation in this Docket are not reasonable and should be modified by the Commission in its Order. My testimony addresses the ratemaking concepts and procedures that are being recommended by AIC as well as specific rate case adjustments that are needed upon continuation of annual formula ratemaking.

48 **Q. Please summarize the recommendations that are set forth in your testimony.**

49 A. My testimony addresses several issues impacting the determination of Ameren's
50 asserted revenue requirement for 2013 under the proposed formula rate and the
51 "true-up" of such revenue requirements within annual reconciliation procedures that
52 are to be applied under the Act. I explain the test year approach employed to
53 develop the annual revenue requirement changes pursuant to the formula and why it
54 is essential that an average rate base and other test year values be used to determine
55 AIC's actual revenue requirement in the reconciliation procedure in each future
56 year. My testimony also addresses the interest rate that should be applied to over or
57 under-recoveries of AIC's revenue requirement when reconciliation calculations are
58 performed. The balance of my testimony then focuses upon and recommends
59 specific ratemaking adjustments to ensure that 2013 formula-based rates are just
60 and reasonable.

61 With regard to Cash Working Capital ("CWC"), I recommend the conduct
62 of additional studies to improve the accuracy of the estimated revenue collection lag
63 and sponsor immediate revisions under AIC's flawed method now being used to
64 estimate the revenue collection lag, so as to reduce the overstatement of CWC being
65 proposed by the Company. I also propose utilization of AIC's calculated revenue
66 lag associated with Pension expenses, which have been inexplicably ignored in the
67 Company's lead lag study. I also revise Ameren's proposed lead/lag calculations
68 that apply a revenue lag to pass-through tax and I correct Ameren's treatment of
69 income tax expenses in calculating CWC.

70 I also propose several adjustments to test year operating revenues and
71 expenses in my testimony. I recommend full, 100 percent revenue crediting of Late

Payment (also known as Forfeited Discount) revenues in determining the Company's electric delivery service revenue requirement. I sponsor expense adjustments to recognize State income tax rate change savings within deferred income tax expenses and to disallow certain lobbying expenses. I also recommend removal of CWIP from rate base where AIC has no cash investment because project costs were financed by Accounts Payable.

Q. What information have you relied upon in formulating your recommendations?

A. I have relied upon AIC's pre-filed testimony and exhibits in this Docket, as well as the Company's responses to data requests submitted by Staff, the AG and other parties. I have also referenced a copy of 220 ILCS 5/16-108.5 of the Public Utilities Act, which was provided to me by AG counsel. I also rely upon my prior experience with the regulation of public utilities over the past 34 years, including significant experience in Illinois and with alternative forms of regulation for telephone and energy utilities.

Q. Have you prepared any accounting schedules to summarize the adjustments being proposed in your testimony and by Mr. Effron?

A. Yes. AG/AARP Exhibit 1.3 is a seven page summary of the revenue requirement revisions being proposed by Mr. Effron and me. The first page of the Exhibit sets forth the Company's asserted formula revenue requirement from Ameren Exhibit 1.1. Adjustments are then posted in columns to the right of Ameren's asserted values, with supporting calculations appearing on subsequent pages, as referenced in the headings for each column. The sum of Mr. Effron's proposed adjustments is inserted at column (i) on page 1. It should be noted that Mr. Effron and I have not,

with available time and resources, been able to conduct a complete review of all aspects of the Company's filing. As a result, the limited adjustments we are proposing should be viewed as cumulative with the work and recommendations of Commission Staff and other parties' witnesses.

II. TEST YEAR PRINCIPLES AND USE OF AVERAGE RATE BASE IN THE RECONCILIATION.

Q. What is the purpose of a "test year" in the determination of public utility revenue requirements?

A. Energy utilities' rates have traditionally been regulated based upon their annual cost to provide service, including an opportunity to earn a reasonable return on invested capital. The process used to evaluate and measure the cost of service and resulting revenue requirement is the rate case, in which a balanced review of jurisdictional expenses, rate base investment, the cost of capital and revenues at present rates can be undertaken at a common period in time, referred to as a "test year." The proper selection and consistent application of the test year is critically important, so that all of the components of the revenue requirement, including rate base, operating expenses, capital costs and sales or billing determinants are holistically analyzed and quantified in a balanced and internally consistent manner with appropriate "matching" of costs and revenues.

Q. Are there several commonly employed types of rate case test years?

A. Yes. The two broad categories of test years include "historical" test years that employ actual recorded financial information to develop the revenue requirement and "future" and "forecasted" test years that employ projections of expected future

financial information to develop the revenue requirement. Within these two broad categories, the test year calculations can be based upon either an “average” set of rate base and income data throughout the 12 months of the year or, alternatively, an “end-of-period” or “annualized” approach that adjusts one or more elements of the revenue requirement calculation to cost and revenue levels extant at year-end.

Q. What type of test year has been proposed by Ameren in the determination of its asserted formula rate revenue requirement for the 2013 rate year?

A. The Company’s proposed test year is a hybrid, employing both historical and forecasted information and both average and year-end information, as more fully explained in the Direct Testimony of Mr. Stafford.¹ The Company’s proposed rate base is measured as of December 31, 2011, and then is increased for projected plant additions and for projected growth in Accumulated Depreciation through December 31, 2012. The Company has generally quantified the individual elements of rate base as of test year-end, except for CWC that is quantified by lead/lag study and Customer Deposits balances that are quantified as a 13-month average.² Thus, for rate base, Ameren proposes use of both historical and projected data and both average and year-end quantification of specific rate base elements.

Ameren’s test year operating income for ratemaking purposes is based generally upon historical, average amounts as recorded in calendar 2011. Operating expenses and depreciation/amortization expenses start at recorded calendar year levels, with certain adjustments to account for cost recoveries through other tariff mechanisms or to exclude costs not allowable for ratemaking purposes.³

¹ Ameren Ex. 1.0, pages 18-25.

² *Id.* p. 25-32. See also Ameren Ex. 1.1, Schedule FR B-1 and referenced sources therein.

³ Ameren Ex. 2.0, p. 25-33; Ameren Ex. 1.1, Sch. FR C-1 through Sch. FR C-4.

Exceptions to this historical, average approach include projections of depreciation expense associated with Ameren's projected plant in service additions and for income tax expenses that are calculated applying statutory tax rates to a calculation of ratemaking taxable income.⁴

Q. Will the revenue requirement and new rates resulting from Ameren's 2013 rate year formula rate changes later be subjected to reconciliation and "true-up" provisions under Section 16-108.5?

A. Yes. Each May 1, Ameren intends to file its calculation of prospective changes to the formula rate revenue requirement using inputs from the prior year's FERC Form 1 and other data sources. As part of this filing, Ameren would then also calculate a reconciliation to "true-up" the previously approved revenue requirement, which had incorporated projections of changes in plant investment, accumulated depreciation and depreciation expense, to determine a revised revenue requirement for the same period using then available actual recorded data.

Q. Has Ameren proposed any particular test year approach for calculation of the reconciliation revenue requirement?

A. There is no discussion of reconciliation test year concepts in the Company's prepared testimony, but the reference appearing in Ameren Ex. 1.1 at Schedule FR A-1-REC, line 11 indicates the Company's intent to again use a year-end rate base to calculate the reconciliation revenue requirement so as to "true-up" previously approved revenue levels.⁵

⁴ Ameren Ex. 1.1, Sch. FR C-2, line 10 and Sch. FR C-4, lines 1-5.

⁵ Ameren Ex. 1.1, Schedule FR A-1-REC at line 11 indicates an intended "Source" for the "Rate Base-Reconciliation" value would be Schedule FR B-1 at line 36, which amount is the sum of recorded year-end Rate Base balances, prior to projected Plant additions for the subsequent year.

164 **Q. Is it appropriate to employ a year-end rate base in calculating the**
165 **reconciliation revenue requirement that would “true-up” costs using actual**
166 **information?**

167 A. No. The reconciliation calculation should employ an average rate base to properly
168 quantify the return on investment elements of the revenue requirement. The proper
169 level of return for investors should be based on the actual level of capital invested in
170 the delivery service business throughout the true-up period. Adoption of Ameren’s
171 proposed reconciliation approach, that would apply the allowed rate of return to
172 year-end rate base, would systematically overstate the true-up rate base and
173 resulting reconciliation revenue requirement. AIC’s investment in assets serving
174 delivery service customers is generally higher at year-end than throughout the
175 reconciliation year.

176 **Q. Does Ameren’s decision to be a “Participating Utility” under Section 16-108.5**
177 **cause the decision regarding use of an average versus year-end rate base in the**
178 **reconciliation to be an important issue?**

179 A. Yes. The Company is committing to making significant incremental investments in
180 electric system upgrades over the next ten years, including incremental spending for
181 both electric system upgrades and smart grid deployment. These “incremental”
182 investments totaling \$625 million are above and beyond Ameren’s normal pace of
183 spending to accommodate replacement of aging plant, customer growth and other
184 ongoing capital programs. If we assume ratable capital spending and the impact of
185 only the incremental investment commitments in years one through ten of the
186 program, annual rate base growth caused by the new investments could average

about \$62 million per year.⁶ The “value” of reconciling the revenue requirement using year-end versus average rate base would be approximately one-half the ratable investment growth expected each year, since the mid-point of spending in a typical future year could be at the \$31 million level of plant additions, while by year-end plant additions could total the \$62 million.⁷ Translating this typical rate base difference of \$31 million into revenue requirement would produce additional annual revenues for AIC after reconciliation of approximately \$4.4 million per year.⁸

Q. Does Ameren, in fact, anticipate significant and continuous growth in its ratemaking capital structure in every year of the infrastructure investment plan for which it has prepared projections?

A. Yes. The Company’s confidential response to Staff Data Request No. RMP 1.01, Attachment 2 in Docket No. 12-0001 provided projections showing

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there is no doubt that using a year-end rate base in the reconciliation of annual revenue requirements will overstate charges to customers and inflate the Company’s return on actual investment, relative to the actual cost of capital for the year being examined. I have included a copy of this confidential response as AG/AARP Exhibit 1.4 (Confidential), along with a copy of

⁶ \$625 million / ten years.

⁷ This simplified example ignores changes in other elements of rate base, arising from ongoing capital spending on non-incremental programs, continued growth in Accumulated Depreciation, and changes in Accumulated Deferred Income Taxes and other elements of rate base which are assumed to be largely offsetting in this discussion.

⁸ Based upon Ameren’s asserted pretax overall return rate of %, derived from Ameren Ex. 2.1 as the sum of “Authorized Return” of \$195,559 plus “Incremental Tax Gross-up” of \$109,174 = \$304,773, then divided by “Rate Base” of \$2,168,258 = 14.05%.

the Company's response to AG 3.01 in this Docket No. 12-0293 indicating the previously provided 5-year forecast document is updated annually and an update will not be available until year end.

Q. Can you provide an illustration of how the Company's proposed use of a year-end rate base will inflate the Company's return on actual investment in the reconciliation calculation?

A. Yes. To illustrate the problem, we can assume steady annual growth in future rate base and the corresponding amount of common equity capital in the utility, at a pace of five percent per year spread evenly throughout each year. The following table shows the impact upon equity returns of targeting an assumed nine percent ROR on such a growing rate base,⁹ but then calculating revenue requirements on year-end, rather than average invested capital:

Illustration of Average VS Year-end Rate Base (\$ millions) - post tax return and ROE % difference

Year	<u>Projected Rate Base</u>			<u>Return at 9% on Rate Base</u>		Return Difference	Average Equity @ 54%	ROE Impact
	Beg. Of Year	End of Year	Average	End of Year	Average			
1	2,000	2,100	2,050	189	185	5	1,107	0.41%
2	2,100	2,205	2,153	198	194	5	1,162	0.41%
3	2,205	2,315	2,260	208	203	5	1,220	0.41%
4	2,315	2,431	2,373	219	214	5	1,281	0.41%
5	2,431	2,553	2,492	230	224	5	1,346	0.41%

Section 16-108.5 is very specific about the return on equity ("ROE") required under formula rates. However, when year-end rather than average rate base is used in the reconciliation calculation, the post-tax return available for ROE capital exceeds the intended ROE by approximately 41 basis points each year, adding about \$5 million of return costs, plus the related factor-up for income taxes, to the revenue

⁹ Ameren's rate of return is 8.86% under the Act, and I round it up to 9% for illustrative purposes only. See Ameren Ex. 1.0 at 43.

requirement burden faced by ratepayers. If rate base grows more rapidly than five percent per year, the ROE variance relative to intended earnings levels would be even larger, and vice-versa.

Q. Why does the use of a year-end rate base result in the achieved ROE being higher than the intended ROE?

A. The utility's actual investment in new plant and the corresponding growth in newly invested equity and debt capital tend to grow gradually throughout the year. Therefore, the associated return requirement for such capital also grows gradually throughout the year. If the revenue requirement calculation is improperly based upon the year-end level of such rate base investment, as if that investment were fully incurred on January 1 and existed in all months of the test year, the resulting return requirement is systematically overstated. This is the financial result caused by Ameren's proposal to utilize a year-end rate base within the reconciliation process.

Q. If return requirements are overstated, relative to the actual amounts of capital being invested only gradually throughout a test year, why would regulators ever allow utilization of a year-end rate base?

A. In traditional ratemaking, a revenue requirement is set for a several year period, with no retroactive true-up. Regulators may elect to employ a year-end rate base in an otherwise average test year approach when the rates will be in effect for an undefined future period. This approach can help to reduce the regulatory lag between the test year and the time new rates take effect by approximately six months, which is the difference between the mid-point of an historical test year and year-end. It should be noted that when a year-end or "annualized" rate base is used

by regulators, it is common for other elements of the revenue requirement such as wage rates, employee headcounts, customer counts, depreciation expense and other known changes to be similarly annualized at year-end. The combined impact of such broadly applied annualization adjustments is to reduce regulatory lag.

Q. If AIC’s revenue requirements are to now be annually trued-up, so as to fully recover jurisdictional actual incurred costs, is there any remaining need to address regulatory lag through use of a year-end rate base?

A. No. Traditional test-year regulation involves setting utility rates that remain unchanged until the “next” rate case is filed, causing regulatory lag to exist when cost changes occur between test year rate cases. However, regulatory lag concerns are completely mitigated by the new formula ratemaking regime, where Ameren will be made “whole” with interest for changes in all of its actual jurisdictional costs incurred to provide delivery services in Illinois. When the formula-based revenue requirements, which are inclusive of projected net plant in service additions, are trued-up through the reconciliation process to actual cost levels, any revenue requirement variances are allowed interest charges to be sure that regulatory lag imposes no financial consequences on AIC. In this new regulatory environment, there is absolutely no need for the Commission to permit the use of year-end rate base in the reconciliation calculation as a remedy for regulatory lag because the reconciliation process itself eliminates regulatory lag.

Q. With the new annual reconciliation process in place to true-up Ameren’s asserted revenue requirement to its actual cost levels, does it matter whether the revenue requirement at the inception of formula ratemaking utilizes a year-end versus an average rate base?

273 A. Not particularly. The methodology being used to develop the inception revenue
 274 requirement, such as depicted on Ameren Ex. 1.1 at Schedule FR A-1, is of less
 275 importance to AIC's earnings than the method to be used in the future when
 276 calculating the true-up charges or credits to customers in future reconciliation
 277 proceedings.¹⁰ The revenue requirement that is ultimately payable by ratepayers is
 278 the amount calculated after reconciliation, plus any associated carrying charges on
 279 such over or under-recoveries. The Commission's goal in setting the next year's
 280 inception revenue requirement should be to adopt a revenue requirement calculation
 281 method that closely approximates the ultimate revenue requirement owed AIC upon
 282 reconciliation so as to minimize the size of future reconciliation revenue
 283 adjustments.

284 **Q. In Ameren Ex. 1.1, the Company has proposed a spreadsheet template to**
 285 **document the calculation steps to be employed in administering Rate MAP-P.**
 286 **What changes to this template are needed to ensure that the reconciliation of**
 287 **revenue requirements is performed using an average rate base approach?**

288 A. The simplest revision would be to insert two additional lines at what is presently
 289 identified as Sch. FR A-1-REC in the proposed spreadsheet template. The existing
 290 line 11 of this Schedule now references Sch. FR B-1 at line 36 to insert a year-end
 291 rate base from the current filing made each year. I would insert one additional line
 292 beneath existing line 11 to insert from the prior year's filing the Sch. FR B-1, line
 293 36 recorded year-end rate base as of December 31 of the previous year. Then a
 294 second new line would be inserted to calculate the mathematical average of the

¹⁰ This is not to say that inception rates are unimportant to ratepayers or the utility, where actual monthly bills payable by consumers are directly impacted by inception rate levels and the Company's cash flows are also impacted by the level of inception rates.

prior year-end and current year-end rate base values to quantify an average rate base for purposes of calculating the “Net Revenue Requirement – Reconciliation” on Schedule FR A-1-REC each year.¹¹ Conforming changes would be needed within the Rate MAP-P to effect reconciliation of the revenue requirement on an average rate base approach.

A more complex calculation of the actual average rate base used in reconciliation could be employed, that would require more elaborate spreadsheet template revisions than are recommended above. For example, certain elements of the rate base that are included in the amounts used above are not presently quantified at a single point in time, but are instead based upon 13-month averages or specific calculations, such as customer deposits and CWC. It may be worthwhile in the interest of accuracy to substitute the most currently available 13 month averages or separately calculated CWC amounts within the average rate base amounts being used in reconciliation. These more complex calculations could be ordered by the Commission to be included in a compliance filing from AIC once the more substantive issues involving the reconciliation process are resolved.

Q. Are you responsible for development and presentation of the rate base to be used in calculating the initial formula rate case revenue requirement in this Docket?

A. No. AG/AARP witness Mr. Effron is addressing the rate base issues on behalf of the Attorney General and AARP, except for Cash Working Capital and the CWIP adjustments, which are discussed later in this testimony.

¹¹ It should be noted that Ameren Ex. 1.1 at Sch. FR A-3, at line 1, employs a “DS Rate Base” value from Sch. FR B-1 line 36 for determination of the ROE Collar Computation. The changes proposed herein for derivation of the DS Rate Base on an average basis within Sch. FR A-1-REC should also flow through to the ROE Collar computation.

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318

III. RECONCILIATION INTEREST CHARGES.

319 **Q. Can you explain your understanding of what the reconciliation balance is and**
 320 **how it is calculated?**

321 **A.** Under the formula rate law, the Commission must compare the calculation of the
 322 prior calendar year revenue requirement, using actual recorded input data as
 323 reported on the Company's FERC Form 1, to the corresponding previously
 324 approved revenue requirement for that same period. The Company is then required
 325 to either refund or surcharge this difference in revenue requirement to ratepayers,
 326 plus interest.

327

328 **Q. Please describe the Company's proposal with regard to the application of**
 329 **interest charges to the revenue requirement reconciliation balance.**

330 **A.** Ameren proposes, in its formula rate template, to apply a "Monthly Interest Rate" of
 331 0.738% to the revenue requirement "Variance – Reconciliation Before Interest"
 332 amount calculated on Ameren Ex. 1.1 at Sch. FR A-4, lines 1 through 3. This
 333 percentage represents 1/12 of the calculated Weighted Average Cost of Capital that
 334 is calculated at Sch. FR D-1 and appears at line 29. Thus, AIC is proposing that the
 335 revenue requirement difference arising from the reconciliation process in future
 336 years, whether positive or negative, be allowed to earn the Company's calculated
 337 overall cost of capital, rather than simple interest as provided for in the Act.¹²

¹² The AIC filing in Docket No. 12-0293 does not contain a reconciliation calculation. In its next filing to be made in May 2013, AIC is required to reconcile the 2012 actual revenue requirement to ICC-approved revenue requirement amounts that were effective during 2012.

338 **Q. Does the new Section 16-108.5 of the Act specify the interest rate to be applied**
339 **to the revenue requirement reconciliation balances until such amounts are**
340 **charged or credited to ratepayers?**

341 A. No. Section 16-108.5(d)(1) of the Act states, “Any over-collection or
342 under-collection indicated by such reconciliation shall be reflected as a credit
343 against, or recovered as an additional charge to, respectively, with interest, the
344 charges for the applicable rate year.” However, it does not specify the appropriate
345 interest rate to be used for this purpose.

346 **Q. Should the revenue requirement variances calculated for reconciliation**
347 **purposes be allowed interest at Ameren’s overall cost of capital?**

348 A. No. The amounts in question represent short term assets or liabilities that are to be
349 either charged or credited to ratepayers within the annual rate adjustment
350 mechanism. These balances therefore do not require permanent financing by
351 Ameren, and should not be expected to require new Ameren common stock
352 issuances or parent company equity infusions for financing. There is no basis to
353 assume that incremental equity financing will occur in connection with the annual
354 revenue reconciliations. Therefore, AIC’s proposed interest rate that is based upon
355 its overall cost of capital, including a weighted equity return element, should be
356 rejected.

357 **Q. What would be a more appropriate rate of interest for application within**
358 **AIC’s proposed formula rate template spreadsheet, at Ameren Ex. 1.1,**
359 **Schedule FR A-4, line 4, in the Reconciliation Computation?**

360 A. A short term debt interest rate should be used for this purpose, recognizing
361 Ameren’s ability to access credit markets at favorable cost rates to finance short

term asset investments. For example, the average cost of short term debt to Ameren Corporation was 2.3% in 2011.¹³ An alternative cost rate for consideration is the interest rate Ameren currently pays on customer deposit balances, which is presently zero percent.¹⁴

Q. Would utilization of a short term debt cost rate to calculate interest to be applied to revenue requirement reconciliation balances be beneficial to AIC ratepayers?

A. Yes. Short term debt cost rates have recently remained at historically low levels and tend to be generally lower than the costs of more permanent debt capital most of the time. With the large anticipated infrastructure investments AIC will make pursuant to new Section 16-108.5 and because inflation impacts upon annual operating expenses are not projected beyond test year end in setting formula rates, it is reasonable to expect future reconciliations to often yield balances chargeable to ratepayers. Under these circumstances, a relatively lower interest rate would be beneficial to ratepayers.

Q. Is there another accounting measure that could appropriately be employed to determine the interest cost applicable to revenue requirement reconciliation variances?

A. Yes. The Commission could deem the revenue requirement variances under formula ratemaking to be regulatory assets that represent a deferral of operating expenses to be recoverable (or returnable) in future rate periods. Since operating

¹³ The Ameren Corporation SEC Form 10-K for fiscal year ended December 31, 2011 at page 113 summarizes Ameren parent and Genco borrowings under the Credit Agreements that provide short term debt and liquidity to the corporation. The weighted average interest rate paid on outstanding borrowings in 2011 was 2.30%.

¹⁴ Rate determined by the Commission in Docket No. 11-0793, approved December 21, 2011.

expenses are income tax deductible when incurred by the taxpayer, the deferred income tax balances associated with such expense deferrals could be used to reduce the balance upon which interest is accrued. Application of interest to only the net of income tax balance associated with such deferrals is consistent with the economic reality that income tax savings would be realized from AIC's delayed recovery of tax deductible expenses and would serve to reduce the overall interest burden upon ratepayers by about 40 percent.

Q. Would it be reasonable to deem the revenue requirement reconciliation balances to be deferred operating expenses for this purpose?

A. Yes. The formula-based revenue requirement subject to later reconciliation includes the forecasted amount of all jurisdictional additions to net plant in service within rate base, but does not provide for projections of inflation in the utility's operating expenses. Aside from differences between actual and forecasted net plant in service amounts, the majority of the revenue requirement upon true-up to actual costs is likely to be caused by changes in operating expenses where no cost inflation projections are included.

Q. What changes to Ameren Ex. 1.1, Sch. FR A-4, the formula rate spreadsheet template "Reconciliation Computation," are required in order to apply your recommendations?

A. First, the "Variance" appearing at line 3 should be reduced by associated incremental deferred income taxes using the Company's composite Effective Income Tax Rate, which is derived on Sch. FR C-4, at line 4. The calculation and subtraction of related Accumulated Deferred Income Taxes could be inserted as new lines 4 and 5 on Sch. FR A-4. Then, the "Monthly Interest Rate" on line 4 (to be

renumbered line 6) should be modified to tie to Ameren's current cost of short term debt, to be determined within App 12 of the template.

Q. Did the Commission's Final Order in ComEd Docket No. 11-0721 address the question of using the utility's WACC to calculate carrying charges on any reconciliation balances?

A. Yes. ComEd had proposed use of its WACC as a carrying charge, which is the same position being taken by AIC. This position was rejected by the Commission as noted in its Order:

Regarding our review of the various positions on this issue the Commission shares the concern raised by Staff that using the WACC as ComEd proposes would treat the reconciliation amount like a rate base investment rather than a reconciling item. We also find credence in the point raised by the Company that the reconciliation adjustments will represent significant investments and operating expenses funded by the participating utility.

The Commission recognizes that due to the EIMA timeline for the reconciliation period the interest rate is both short term and long term in nature. As discussed above, the customer deposit rate does not encompass the long term aspect of the time period of the reconciliation. The WACC includes the weighted costs of short-term debt, long-term debt, and common equity. The Company proposes the WACC which is inclusive of the common equity, which does not represent debt on which to set an interest rate. The Commission believes there is value in setting an interest rate based upon debt that is relevant to the Company for the time duration of the reconciliation. In order to capture the unique aspects of the relevant period we find that a hybrid approach should be utilized to determine the appropriate interest rate. Such a hybrid calculation would take the weighted costs of short-term debt and long-term debt and exclude the weighted cost of common equity as the methodology in calculating the interest rate. This results in an interest rate of 3.42%. The Commission concludes that this hybrid interest rate of 3.42% is reasonable and appropriate to be utilized for the reconciliation period and is hereby adopted. [Final Order, page 166]

This “hybrid” approach adopted by the Commission, if also applied to AIC, would avoid any concern regarding a need to specifically assign and track incremental short term debt associated with reconciliation balances

IV. CASH WORKING CAPITAL ISSUES.

Q. Has the Company proposed an allowance for Cash Working Capital (“CWC”) within the rate base used to establish annual formula rates?

A. Yes. Ameren Ex. 1.1 at App 3 is the Company’s proposed calculation supporting an allowance for CWC of \$13,607,000 that is sponsored by witness Mr. Stafford who states, “The CWC calculation is based upon a lead/lag methodology developed in the testimony and supporting workpapers of Ameren witness Mr. David Heintz in Docket No. 12-0001.” According to Mr. Stafford, AIC has proposed to update the leads/lag analysis every three years for purposes of the formula rate and because of this proposal, “...for this initial update filing, only an update of the revenue and expenses for the applicable calendar year, 2011, has been reflected in the determination of cash working capital on App 3.”¹⁵

Q. Did you submit testimony explaining several problems with the lead/lag study that was proposed by Mr. Heintz in Docket No. 12-0001?

A. Yes. In Ameren’s initial formula rate filing, Docket No. 12-0001, as in its most recent rate case, considerable controversy surrounded the lead lag study proposed by the Company. My testimony in Docket No. 12-0001, along with testimony by Commission Staff and other intervenor witnesses, explained certain adjustments

¹⁵ Ameren Exhibit 1.0, page 20, line 402-411.

that must be made to the Company's lead/lag study results before they can reasonably be used to calculate formula rates for Ameren Illinois. These included:

1. Revision of Ameren's estimated revenue collection lag to insert reasonable grace period assumptions, as were used in ComEd's calculations approved by the Commission in Docket No. 10-0467, so as to provide conservatism and recognition of the period within which residential and commercial customers' bills are payable but not delinquent.
2. Reinstatement of the Commission's ordered treatment of pass-through taxes, assigning no revenue lag to these amounts where Ameren serves as the collection agent and not tax is owed until after revenues are collected by Ameren.
3. Removal of lag days assigned by Ameren to income tax expenses, since the Company is in a tax loss carry-forward position and is not currently paying any income taxes in cash, but is instead recording only deferred income tax expenses that are a non-cash expense that does not impact cash working capital.

Q. Has Ameren submitted testimony in support of its lead lag study lag day values?

A. No. In this Docket No. 12-0293, Ameren did not re-submit Mr. Heintz's testimony.

Q. Are you repeating your testimony on these issues in this Docket No. 12-0293?

A. No. Given the Company's apparent intent to rely upon the Commission's resolution of lead/lag study issues from Docket No. 12-0001 for determination of lag day values to apply to updated test year income statement inputs on a three year

cycle, I am not repeating the detailed testimony supportive of the AG/AARP adjustments to the lead/lag study. Instead, I have included copies of my Direct Testimony that was filed in Docket No. 12-0001 as AG/AARP Exhibit 1.5, and have incorporated the lead/lag day values I sponsored in that prior Docket in calculation of the updated CWC amount in this revenue requirement update Docket No. 12-0293. While the specific dollar figures referenced in Docket No. 12-0001 are not applicable to the CWC calculations in this docket, the rationales for Commission adoption of these lag day adjustments remain the same and should be applied here.

Q. Have you prepared an Exhibit to summarize the changes you are recommending to Ameren's CWC calculations?

A. Yes. AG/AARP Exhibit 1.3 at page 2 is a spreadsheet calculation that reformats and summarizes Ameren's lead/lag study Ex. 1.1, App.3, to show the line by line impact of each cost element included in the Company's lead/lag study. I have included the effect of each lead/lag study adjustment I recommended in Docket No. 12-0001 within this calculation. Lines 1 through 17 and columns (a) through (g) of my Exhibit replicate the Company's results on Ameren Ex. 1.1 App. 3, but combine the Revenue Lag and Expense Lead for each line items so as to show the overall CWC impact of each element of the analysis. This simplified presentation format is useful in isolating the CWC effects associated with the lead/lag study treatment of each category of transaction.

After this restatement of the Company's study, I present at columns (h) through (l), a side-by-side calculation showing each change I am proposing to

illustrate the resulting differences in CWC. The cells in columns (h) and (i) are shaded where an AG/AARP change to study inputs has been made. This same format can be used to insert the Commission's decisions in Docket No. 12-0001 regarding appropriate lead/lag day values for each line item, as well as updated final approved operating expense and other cash flow amounts in column (b).

V. LATE PAYMENT REVENUE ALLOCATIONS.

Q. What are Late Payment Charge revenues and how have they been treated in this AIU formula rate update filing?

A. Late Payment Charges are added to ratepayers' bills when payments have not been received by the due dates of the bills. AIU Electric Service Schedule III. C.C No.1, Original Sheet No. 3.018 provides for a "...late payment charge equal to 1.5% per month will be assessed on any amount considered past due," as more fully described in the tariff. In 2011, Ameren recorded as "forfeited discounts" in Account 450 total late payment revenues of \$12.043 million, as shown at Ameren Ex. 1.1, page 28, line1 within App 10. However, the Company applies a "revenue" based allocation factor of 45.56% which results in only \$5.487 million of the total recorded late payment revenues being recognized for ratemaking purposes. This reduced value after allocation is carried then forward as part of the total of \$34.5 million of Other Operating Revenues from line 14 of App 10, for inclusion as a revenue credit to the overall revenue requirement at Ameren Exhibit 1.1, page 1 (Sch. FR A-1) at line 21.

534 **Q. What will happen to the other 54.44% of the AIC late payment revenues that**
 535 **the Company seeks to treat as non-jurisdictional for ratemaking purposes in**
 536 **its Exhibit 1.1?**

537 A. The balance of late payment charge revenues not being credited to reduce the
 538 revenue requirement will be retained by shareholders, because no other regulatory
 539 jurisdiction would receive any revenue credits for this other 54.44% share.

540 **Q. Was AIC's proposed allocation of more than half of late payment revenues a**
 541 **disputed issue in Docket No. 12-0001?**

542 A. Yes.

543 **Q. Why has Ameren not recognized the other 54.44 percent of recorded late**
 544 **payment charge revenues that it earned in 2011 in determining the AIC**
 545 **revenue requirement under formula rates?**

546 A. The Company's was asked this question in data request AG 2.12 and the response
 547 stated is, "See the Company's response to AG 3.03." In its response to AG 3.03,
 548 the Company appears to have created several new fictional regulatory jurisdictions
 549 that it calls, "Production, Transmission and Other." However, in the same response
 550 Ameren is unable to explain or provide citation to any ICC orders or other
 551 documents showing how revenue credits for late payments charges have ever been
 552 recognized in determining rates within any of these imagined new jurisdictions.

553 In its response to AG 3.02 AIC attempts to rationalize its retention of more
 554 than half of late payment revenues by suggesting inadequacies within several cost
 555 recovery tariffs, including:

- 556 • Pension and post retirement costs from Ameren Illinois production retirees.

- Risk reduction in ROE approved by the ICC in Docket 09-0306 cons. associated with the existence of Rider EUA that recovered electric power supply uncollectible expense.
- Cash lag between the provision of transmission service and receipt of payment.
- “Other” costs including but not limited to uncollectibles, energy efficiency and demand response, manufactured gas cleanup costs, and add on/revenue taxes.

After listing these areas of suggested cost under-recovery, AIC provides no evidence that past ICC decisions disallowing production retiree costs, establishing and administering rate riders or findings regarding risk reductions to ROE were improper or inadequate. Notably, Ameren admits in its response to AG 3.02 that it has not conducted any analysis or review to determine whether any costs in these other phantom jurisdictions have been denied recovery or that such denial warrants retention of late payment revenues as compensation.

Q. Should AIC be allowed to retain the majority of late payment revenues to offset previous ICC ratemaking decisions or to remedy alleged cost under-recoveries from ICC-regulated rate riders?

A. No. It would be unfair to ratepayers to reward Ameren shareholders with millions of dollars in annual late payment revenues in order to effectively reverse past ICC decisions or to modify existing cost recovery riders based on nothing more than Ameren’s unhappiness with those decisions and disallowances.

Q. Does Ameren provide service in another jurisdiction besides the Illinois Commerce Commission?

581 A. Yes. Wholesale transmission services are regulated by the FERC and AIU submits
 582 annual formula rate adjustment applications with the FERC based upon current
 583 costs and revenues to update its open access transmission rates. When allocations
 584 are aligned or conformed between the ICC and FERC jurisdictions, Ameren will
 585 recover 100% of its costs after consideration is given to expenses, rate base
 586 investments and revenue credits that are available to offset such costs. AIU does
 587 not provide service in any jurisdictions other than the ICC and the FERC.

588 **Q. Does the Company allocate any portion of its late payment revenues to the**
 589 **FERC jurisdiction for ratemaking purposes?**

590 A. No. The Company admitted in its response to AG 3.03(d) that, “None of the
 591 Illinois Forfeited Discount revenues have [been] treated as a revenue credit in
 592 determining Ameren’s FERC transmission revenues in the Companies’ most recent
 593 transmission rate adjustment proceeding.”¹⁶

594 **Q. What is included in AG/AARP Exhibit 1.6?**

595 A. AG/AARP Exhibit 1.6 contains copies of the Ameren responses to data requests
 596 AG 2.12, AG 3.03, AG 3.02 and AG 3.05 that address the jurisdictional treatment
 597 of late payment (aka forfeited discounts) revenues.

598 **Q. Has the Commission previously addressed the proper jurisdictional allocation**
 599 **of late payment revenues in any recent rate case?**

600 A. Yes. In Docket No. 10-0467 ComEd had proposed retaining a substantial share of
 601 its late payment revenues for Exelon shareholders, through application of a
 602 revenue-based allocation factor like that used by AIC. In its final Order, the
 603 Commission rejected the Company’s proposed changes, stating:

¹⁶ See AG/AARP Exhibit 1.6; AIU response to AG 1.07.

ComEd has classified the \$13.986 million as non-jurisdictional. However, as CUB points out, the only “other jurisdiction” that ComEd is subject to is the FERC. Yet clearly, except for \$2 million, which was accounted for by Mr. Effron, these are not FERC-related charges. Additionally, ComEd is in the business of delivering electricity. In that capacity, to many customers, it provides the electricity to deliver. Therefore, whether the late charges are upon delivery charges or upon the electricity delivered, they are imposed to the delivery service that ComEd provides to the individual customer involved.

To illustrate the fallacy of ComEd’s argument, the Commission points out that a consumer’s total bill has many charges, including such items as those for state and local taxes. The interest charge is imposed on all of these charges. Yet, it cannot be said that state and local taxes are non-jurisdictional. The Commission concludes that ComEd has failed to establish, on an evidentiary basis, that a portion of these charges is not jurisdictional.

On Exceptions, ComEd avers that the conclusions above are inconsistent with other instances in which this Commission has found charges to be jurisdictional. (ComEd Brief on Exceptions at 100-101). However, this situation, unlike the other situations, clearly does not involve non-jurisdictional charges.

The Commission further rejects ComEd’s argument that, pursuant to AG/CUB witness Brosch’s approach, retail electric suppliers’ customers would receive an unfair “advantage,” due to the fact that they are subject to a lesser charge to ComEd (but one that will undoubtedly also be charged by retail electric suppliers). There has been no showing here that the system, which creates the potential for great profit (late payment charges) for bundled service customers who are late, versus a lesser profit for ComEd (use of a retail electric suppliers for the supply of electricity, and, therefore, a lesser amount, upon which, ComEd can charge a late payment fee percentage) creates any “advantage” for retail electric suppliers’ customers. The only “advantage” is that ComEd receives greater profit from bundled customers. The Commission fails to see how receipt of a greater profit from one group of customers could elevate into discriminatory charges, or, any legally-recognized “advantage.” Also, this charge is only imposed upon customers when they do not pay their bills on time. The Commission, therefore, adopts AG/CUB witness Brosch’s adjustment on this issue. [Order p. 306]

The situation with regard to Ameren's late payment revenues is nearly identical to that of ComEd, except that Ameren is not crediting any of these revenues to the FERC jurisdiction for ratemaking purposes.

In deference to the Commission's decision in Docket No. 10-0467, the ComEd formula rate filings in Docket Nos. 11-0721 and 12-0321 recognize 100 percent of its late payment revenues that are not credited to the FERC jurisdiction as a revenue credit in determining the distribution service revenue requirement.

Q. What treatment do you propose with regard to late payment revenues?

A. Late payment revenue should be treated as 100% ICC-jurisdictional and not be subject to any revenue-based allocation factor that would allow Ameren shareholders to retain a portion of such revenues. These amounts are paid entirely by retail ratepayers pursuant to ICC rules and Ameren's Illinois tariff. The Company has made no showing that justifies shareholder retention of such revenues.

Q. Is Ameren inconsistent in its proposed allocation of late payment charge revenues based upon relative production, transmission and delivery service revenues in Ameren Ex. 1.1, App. 10, given its treatment of other customer provided funds?

A. Yes. Customer Deposits are assessed based upon the relative size of anticipated customer bills and such deposits serve to secure payment for all elements of billed revenues, including recovery of power supply (production), transmission and distribution cost recoveries. However, at Ameren Ex. 1.2, page 55 Workpaper 2, Electric Customer Deposit balances are treated as 100 percent jurisdictional in

determining delivery service revenue requirements.¹⁷ This is an appropriate treatment of Customer Deposits and such 100% assignment to retail delivery services should also apply to late payment revenues.

Q. Does the AG/AARP adjustment to Other Revenues appearing in column (d) of your AG/AARP Exhibit 1.3 include a reversal of the AIU proposed jurisdictional allocation of late payment revenues?

A. Yes. A more detailed calculation of the adjustment I proposed is set forth at page 3 of AG/AARP Exhibit 1.3.

VI. STATE INCOME TAX RATE ISSUE.

Q. Has Ameren recognized the higher Illinois corporate income tax rate that is effective in 2011?

A. Yes. Ameren Exhibit 1.1 at Schedule C-4 reflects utilization of the new higher 9.5% Illinois State Tax Rate at line 2, to calculate the “Incremental Tax Gross Up Factor” that is used on Schedule FR A-1 at line 16. Unfortunately, the Company’s calculations assume that AIC will experience taxable income and actually pay taxes at these higher rates, even though all of the Company’s current state income tax obligations in 2011 are deferred into future years.

Q. Are Illinois State Income Tax rates scheduled to remain at the higher 9.5% corporate income tax rate in all future years after 2011?

¹⁷ Ameren Part 285 Schedule WPB-13b also shows the attribution of 100% of Electric Customer deposits and a revenue-allocated share of Common Customer Deposits (Customers purchasing gas and electric services from AIC) are included in rate base.

694 A. No. The corporate income tax rate is scheduled to drop back to 7.75% in 2015 and
 695 then drop back to the original 7.3% rate in 2025.¹⁸

696 **Q. Will the scheduled reduction in future Illinois State Income Tax rates result in**
 697 **some income tax savings to Ameren?**

698 A. Yes. AIC tax deductions taken today will produce income tax deferrals today when
 699 tax rates are at the higher 9.5% rate, creating book/tax timing differences and
 700 deferred income taxes today that will reverse in future years, at which time income
 701 taxes will then become payable at the lower tax rates scheduled to be effective at
 702 that time. This phenomenon is completely ignored in Ameren's filing, but is the
 703 subject of specific large ratemaking adjustments in ComEd's formula rate update
 704 filing in Docket No. 12-0321.

705 **Q. How does ComEd explain the ratemaking implications of the temporary**
 706 **increase in corporate state income tax rates?**

707 A. In the ComEd filing, witness Mr. Fruehe testifies as follows:

708 **Q. How did the increase in the Illinois income tax rate in 2011 impact**
 709 **the revenue requirement?**

710 A. The passage of Illinois Senate Bill 2505 on January 13, 2011 increased
 711 the previous corporate income tax rate of 7.3% to 9.50% for the years
 712 2011 through 2014, with reductions to 7.75% in 2015 and 7.3% in 2025.
 713 This change impacts the revenue requirement in several ways.

714 First, the statutory state income tax rate used to calculate the
 715 overall total income tax rate on Schedule FR C-4 has been revised to
 716 reflect the 9.5% statutory state income tax rate.

717 Second, as a result of the change in the rate, previously recorded
 718 accumulated deferred income tax balances, i.e. balances as of December

¹⁸ 35 ILCS 5/Art. 2. Available at:
<http://www.ilga.gov/legislation/ilcs/ilcs4.asp?DocName=003500050HArt%2E+2&ActID=577&ChapterID=8&SeqStart=600000&SeqEnd=3100000>

31, 2010, were required to be remeasured to reflect the deferred tax balances calculated by applying the new tax rates noted above. The remeasurement of ADIT resulted in a required increase to jurisdictional ADIT as of January 1, 2011 of \$13.1 million. Consistent with prior ICC guidance (ICC Docket No. 83-0309, addressing the manner in which deferred tax impacts resulting from tax rate changes should be addressed), this shortfall in ADIT is offset by a regulatory asset and is being amortized prospectively over the remaining life of the underlying assets by applying a weighted-average rate method for future reversals. Amortization of the remeasurement balance was a credit of \$1.9 million in 2011.

Finally, in 2011, ComEd recognized a significant benefit due to the difference between the current income tax rate of 9.50% and the rate at which the related deferred tax expense is recorded. The deferred tax rate is lower because, as described above, the state income tax rate is scheduled to decline in 2015 and again in 2025, which means that some of the deferred taxes recorded in 2011 will reverse in later years when the state income tax rate is scheduled to be lower. This difference in current and deferred tax rates, combined with the fact that during 2011 ComEd had two notable and significant tax deductions (100% bonus depreciation and the expense related to the adoption of the T&D repairs safe harbor methodology) resulted in a 2011 tax benefit of \$16,960,000 (jurisdictional), which is included in the tax adjustments shown on Schedule FR C-4.

Q. Were the income tax expense adjustments that are proposed by ComEd due to lower future stated income tax individually significant?

A. Yes. The third adjustment described in the paragraph of Mr. Fruehe's testimony that begins with the word "Finally" is quite significant, resulting in a 2011 income tax expense benefit of \$16.9 million. This adjustment is quantified at ComEd Ex.

3.2, WP 9, page 2 of 4 and results from utilization of lower income tax rates to calculate deferred income tax expenses in 2011, in anticipation of reversal of book/tax timing differences in future years when state income tax rates are scheduled to be lower.

Q. Do the State Income Tax rates and Generally Accepted Accounting Principles that apply to ComEd apply equally to AIC?

A. Yes. While the specific tax deductions, tax credits and income levels are obviously unique to each of the two utilities, there is no reason why only ComEd is able to benefit from the expected turnaround of tax deferrals in future, lower-rate tax periods. Ameren offers no testimony or calculations indicating how the changing Illinois state income tax rates will impact its ADIT accounting or recorded deferred income tax expenses.

Q. How does AIC explain the absence of deferred income tax expense adjustments comparable to those included in ComEd's formula rate filing?

A. In its response to data request AG 2.04, reference was provided to the ComEd tax rate adjustments and the Company was asked to explain the omission of comparable adjustments in its filing in Docket No. 12-0293. In its response to part (d) of this question, the Company states, "See AG 2.04 Attach 2 which identifies only the schedule m's that were booked during the normal course of the year with a difference between current and deferred income tax expense. The jurisdictional amount is a reduction to income tax expense of \$27,995." In response to part (e) of this data request, the Company states, "AIC is not proposing ratemaking treatment of the state income tax rate differential impacting ADIT, as quantified in response to part (d), based on past practice of the Commission in calculating income tax

expense at statutory rates. I have included a copy of this data request response as AG/AARP Exhibit 1.7.

Q. How can Ameren’s quantification of this adjustment at only \$27,995 be so much lower than ComEd’s \$16.9 million income tax expense adjustment?

A. Under the accelerated procedural schedule in this Docket, it has not been possible to critique the Company’s response or submit follow-up discovery prior to finalizing this testimony, but I suspect that AIC’s decision to restrict the analysis to what it calls, “schedule m’s that were booked during the normal course of the year” caused a lower value to be assigned to this issue. The “schedule M” book/tax timing difference items listed in AIC’s AG 2.04 Attach 1 spreadsheet include only certain of the smaller book/tax timing differences, with no recognition being given to the large bonus depreciation, repairs deduction and other property-related book/tax differences that were clearly included in ComEd’s analysis. AIC Schedule C-5.3 at page 2 summarizes “Differences Between Book and Tax Depreciation” in 2011 that total \$218.5 million” which represent plant-related book/tax differences that will inevitably reverse over many future years, including years after state income tax rates are scheduled to decline. The Commission should require a complete accounting for changing state income tax rates and deferred income tax expense savings from Ameren, to ensure ratepayers are not denied the permanent income tax savings that arise from such changing income tax rates.

Q. Have you been able to verify that AIC is deferring large amounts of State Income Taxes in 2011?

A. Yes. At Schedule C-5a, page 3, line 65, calendar year State Income Tax expenses that are currently payable are negative \$16.3 million, while State Deferred Income

Taxes are positive \$28.3 million. This means that AIC's current State taxable income is negative, because tax deductions and tax credits exceed taxable revenues. Yet the company's revenue requirement will recover large amounts of "deferred" income taxes that will serve to reduce rate base until such amounts become payable in future tax years.¹⁹

Q. Please explain the adjustment appearing on AG/AARP Exhibit 1.3 at page 4.

A. I am proposing an adjustment as a place holder for the more specific calculations that should be required of Ameren in order to quantify the needed ratemaking adjustments that are comparable to ComEd's adjustments. The \$6,127,597 million place-holder adjustment for this purpose is taken from AIC Schedule C-5.2, page 3 at line 63 which is captioned "IL Rate Change" in the "Electric" column of the Company's Schedule. It is not obvious from Schedule C-5 whether this amount is indicative of deferred income tax expense savings from scheduled future state income tax rate reductions or why this amount is completely eliminated in the "Other" column, so as to yield a zero amount in the Jurisdictional column.

Q. Has the AG submitted additional discovery on this topic in an effort to either confirm the accuracy of the \$6,127,597 amount or to more specifically quantify the required adjustment?

A. Yes. However, responses to those requests are pending.

¹⁹ Normalization accounting that is practiced for accelerated tax depreciation and other book/tax timing differences requires the provision of deferred income taxes on the books and the corresponding inclusion of such deferred income tax expenses for ratemaking purposes. In future years, when these timing differences "reverse" and, for example, book depreciation exceeds tax depreciation, the recorded balance of deferred taxes for that timing difference is amortized to offset incrementally higher taxes that are then currently payable.

VII. OPERATING EXPENSE ADJUSTMENTS.

A. Lobbying Expense

Q. What is the purpose of the adjustment you propose at AG/AARP Exhibit 1.3, page 5?

A. This adjustment reduces recorded expenses for the portion of Edison Electric Institute dues in the test year that were incurred for the purpose of influencing legislation. The quantification of this adjustment was outlined in AIU's response to AG 3.10, a copy of which has been included in AG/AARP Exhibit 1.8.

Q. Has Ameren proposed its own adjustment to exclude lobbying expenses incurred in the test year?

A. Yes. A small adjustment is proposed by Ameren to remove lobbying costs incurred directly by Company employees, as detailed in Ameren Ex. 1.2, page 119 as part of Workpaper 7. This small adjustment is posted at Ameren Ex. 2.1, page 23 (App 7) at line 11. The additional EEI dues adjustment I propose is necessary to more completely reclassify AIU's lobbying activities and expenses to below the line accounts to be borne by shareholders rather than ratepayers.

B. Corporate Branding Expenses

Q. Please describe the adjustment appearing at page 6 of AG/AARP Exhibit 1.3.

A. In its Schedule WPC-8, AIU provided a detailed breakdown of its 2011 advertising, corporate branding and event sponsorship expenses. The adjustment I propose would remove expenses incurred to conduct image advertising under Ameren's new "Focused Energy for Life" campaign. Line 2 proposes a small additional adjustment to exclude expenses incurred to provide corporate branded merchandise within an internal store for employees. These expenses are not reasonable or

necessary for the provision of utility services and should be excluded in setting rates. Line 6 of this adjustment removes expenses incurred by Ameren for corporate sponsorship of community and sporting events that are discretionary expenses not required for the provision of utility services.

Q. Why should the Company’s “Focused Energy for Life” slogan and advertising, as referenced at AG/AARP Exhibit 1.3, page 6, line 1, not be funded by utility ratepayers?

A. This type of image enhancement advertising is not necessary to provide regulated delivery service and appears to be intended to promote favorable public opinion of Ameren at ratepayers’ expense. According to Schedule WPC-8 at page 18, “In 2011, Ameren introduced the corporation's promise, *Focused Energy. For Life.*—it means that we’re focused on making sure the energy vital to life will be there, today and for generations to come. This was a significant efforts [sic] to determine the new promise and to implement the promise reflecting in all company related collateral.” This page of WPC-8 indicates that its “Focused Energy for Life (FEFL)” campaign originated from Ameren’s “Identity & Education Initiative” and is intended to “Create stronger relationships with customers, communities, co-workers and other stakeholders” and to “Educate and inform stakeholders on issues of importance.”

Q. Why is such image-building or goodwill advertising not properly included in utility revenue requirements?

A. Customers need not pay for advertising that reminds them that the utility provides electric delivery services around the clock or that electricity is essential to living. If Ameren elects to incur costs in an effort to enhance its public reputation and to

remind customers that it is doing its job, these discretionary expenditures should not be included in the revenue requirement. Ameren has made no showing that these expenses are prudent, necessary or cost effective in meeting its public utility service obligation.

VIII. CONSTRUCTION WORK IN PROGRESS.

Q. What is the purpose of the adjustment you proposed at AG/AARP Exhibit 1.3, page 7?

A. Ameren has included a list of projects that were included in its balance of CWIP not earning AFUDC as of December 31, 2011. These projects are listed at Ameren Ex. 1.2, page 177 at Workpaper 15, with the total of \$831,476 being proposed for rate base inclusion. The Company has identified Accounts Payable related to several of the listed projects, as set forth at lines 1 and 2 of AG/AARP Exhibit 1.3, page 6, which means that vendors rather than shareholders have funded these CWIP investments as of year-end. To recognize this non-shareholder funding for CWIP, I have quantified the adjustment needed to reduce Ameren's asserted rate base for CWIP not subject to AFUDC that has not been funded by AIC investors.

Q. How did you determine which of AIC's CWIP projects were funded by Accounts Payable?

A. In its response to AG 3.13, the Company provided the necessary information to quantify this adjustment. I have included a copy of this response in AG/AARP Exhibit 1.9.

Q. Has the Commission previously concluded that CWIP allowed into rate base should be reduced to account for related Accounts Payable balances?

892 A. Yes. In its order in ComEd Docket No. 10-0467, the Commission stated:

893 ...It appears that there was no attempt on the part of ComEd to
 894 determine what, if any, of these smaller projects are funded by the lag
 895 between the time when they are booked and when the bills for these
 896 items/payment to employees or contractors are actually paid. As the
 897 AG and CUB point out, many of these items can be temporarily
 898 financed by time. Additionally, the AG asserts that ComEd's lead/lag
 899 study does not include CWIP-related items and ComEd's evidence
 900 provides no specifics indicating that the AG or Mr. Brosch are wrong
 901 in this regard.

902 While Ms. Houtsma's testimony in this regard is vague, the
 903 Commission cannot conclude that it is inadmissible as a matter of law.
 904 (e.g., Fraley v. City of Elgin, 251 Ill. App. 3d 72, 76-77, 621 N.E.2d
 905 276 (2nd Dist. 1993), discussing when factual conclusions are totally
 906 unsupported factually, and therefore may be disregarded, as a matter of
 907 law). \$12.6 million is at issue, and it concerns many, many, small
 908 projects that can be completed quickly. The Commission also cannot
 909 state, within a reasonable degree of certainty, that all of these projects
 910 are vendor-financed. The Commission appreciates the fact that
 911 accrual-based accounting records record items that will become due
 912 and owing in the future, as opposed to when the bills for those projects
 913 become due and owing. The Commission also appreciates the fact that
 914 there can be a lag between when work is performed and when the bill
 915 for that work is paid. However, without evidence indicating that these
 916 two lags allow ComEd to pay for its CWIP-related projects, the
 917 Commission cannot state, within a reasonable degree of certainty, that
 918 ComEd's CWIP-related projects are financed by these two lags.

919 *However, in ComEd's next rate case, any lead/lag study shall*
 920 *include the effect of accrual accounting on payment for its smaller*
 921 *CWIP-related payments (the payments that are at issue here and that*
 922 *are not accounted for with AFUDC). Failure to do so could result in a*
 923 *determination that ComEd did not meet its burden of proof, or, that*
 924 *ComEd failed to comply with a Commission Order, with all of the*
 925 *penalties that are provided for such failure in the Public Utilities Act.*

926 Docket No. 10-0467, Order of May 24, 2011 at 30-31 (emphasis added)

927 **Q. Is your adjustment to CWIP consistent with the Commission's conclusions**
 928 **quoted above?**

929 A. Yes.

930 **IX. CONCLUSION AND RECOMMENDATION.**

931

932 **Q. What is your recommendation regarding the initial revenue requirement to be**
933 **determined for Ameren in this Docket?**

934 A. I recommend that AIC's delivery service revenue requirement be found to be no
935 larger than the amount shown in AG/AARP Exhibit 1.3, at page 1, line 25 in
936 column (j). This amount should be further modified for any Commission-approved
937 ratemaking adjustments proposed by the Staff and other parties, that are not
938 addressed in my or Mr. Effron's Direct Testimony.

939 **Q. Does AG/AARP Exhibit 1.3 also include the impact of adjustments being**
940 **proposed by Mr. Effron?**

941 A. Yes. Page 1, column (i) of AG/AARP Exhibit 1.3 reflects the overall adjustment to
942 rate base being supported by Mr. Effron.

943 **Q. What do you recommend regarding the Company's proposed formula rate**
944 **template set forth at Ameren Exhibit 1.2?**

945 A. The AIU formula rate template should be modified as necessary to comport with the
946 ratemaking decisions reflected in the Commission's Order in this Docket.
947 Corresponding changes to proposed Rate MAP-P should also be submitted in an
948 AIU compliance filing, subject to review by Staff and other parties, prior to the new
949 formula rate tariff being made effective.

950 **Q. Does this conclude your testimony at this time?**

951 A. Yes.
952